

GAO

Report to the Administrator, Agency  
for International Development

**AD-A270 498**



February 1991

# INTERNAL CONTROLS

## AID Missions Overstate Effectiveness of Controls for Host Country Contracts



**93-23464**



GAO

United States  
General Accounting Office  
Washington, D.C. 20548

National Security and  
International Affairs Division

B-242452

February 11, 1991

The Honorable Ronald W. Roskens  
Administrator, Agency for International  
Development

Dear Dr. Roskens:

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At the request of the Chairman, Subcommittee on Oversight of Government Management, Senate Committee on Governmental Affairs, we reviewed the Agency for International Development's (AID) policies and procedures for host country contracting. During our ongoing review, we found some managerial concerns that warrant your attention and therefore are being reported directly to you. This report focuses on whether AID missions in Bangladesh, Egypt, Jordan, and Pakistan accurately reported to AID/Washington the status of existing internal controls for host country contracts. A separate report is being prepared for the Senate Subcommittee to address our overall assessment of AID's management and oversight of host country contracts.

## Background

Under a host country contract, AID gives a host government agency responsibility for both contract award and implementation—subject to AID oversight and contract approval. As of October 1989, AID reported that active host country contracts totaled \$1.5 billion, or 56 percent of AID's total awards for overseas project assistance. The four missions we visited accounted for approximately 75 percent of AID's total expenditures for host country contracts.

The Federal Managers' Financial Integrity Act of 1982 requires the head of each federal agency to annually report to the President and the Congress on whether internal controls are operating effectively. Any material weaknesses in internal controls must be noted.

AID's annual certification is based on individual certifications filed by its overseas missions and other agency components each year. From 1987 through 1989, missions' certifications were mainly based on their responses to an internal controls questionnaire distributed by

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AID/Washington. The questionnaire incorporated specific control techniques designed to measure missions' compliance with AID's payment policies<sup>1</sup> and other oversight requirements for host country contracts.

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## Results in Brief

In their 1988 and 1989 certifications to AID/Washington, the missions we visited did not accurately portray the status of selected internal controls relating to host country contracts. In 21 of 47 instances in which control techniques were rated as "satisfactory" or "not applicable," the missions overstated the quality or effectiveness of their controls. Controls were rated "satisfactory" or "not applicable" by mission personnel without sufficient justification or despite negative information that should have led to an "unsatisfactory" rating.

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## Control Techniques Rated Satisfactory Without Sufficient Justification

To complete the internal controls questionnaire, missions had to rate control techniques as "satisfactory," "unsatisfactory," or "not applicable" based on general knowledge or detailed testing. AID required that missions test selected control techniques at least once during the 3-year review cycle.

Guidelines issued by the Office of Management and Budget state that assessments of control techniques should be supported by review documentation showing the type and scope of review, the responsible official, the pertinent dates and facts, the key findings, and the recommended corrective actions.

At the four missions visited, we examined the 1988 and 1989 assessments of seven control techniques relating to AID's oversight of host country contracts. In each case, we reviewed available documentation and assessed whether a control technique was adequate. The results of this comparison are shown in table 1. Differences between the missions' and our evaluations are highlighted. The first four techniques listed in table 1 relate exclusively to host country contracts, while the last three apply to host country and other forms of contracting.

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<sup>1</sup>In December 1983, AID consolidated many of the oversight and monitoring tasks associated with host country contracting in its payment verification policies.

**Table 1: AID Missions' and GAO's Assessments of Selected Control Techniques**

Control technique	Fiscal year	Bangladesh		Egypt		Jordan		Pakistan	
		AID	GAO	AID	GAO	AID	GAO	AID	GAO
1. Evaluate the contracting and contract management abilities of all host agencies responsible for AID-funded contracts.	1988	<b>S</b>	<b>U</b>	<b>S</b>	<b>U</b>	<b>S</b>	<b>U</b>	<b>S</b>	<b>U</b>
	1989	<b>S</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>S</b>	<b>U</b>	<b>U</b>	<b>U</b>
2. Monitor the host agency advertising, award, and contract negotiation procedures.	1988	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>	<b>S</b>	<b>S</b>
	1989	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>	<b>S</b>	<b>S</b>
3. Review host agency invoice examination procedures.	1988	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>
	1989	<b>S</b>	<b>S</b>	<b>U</b>	<b>U</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>
4. Ensure host country contracts are audited.	1988	<b>S</b>	<b>U</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>	<b>NA</b>	<b>U</b>
	1989	<b>S</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>S</b>	<b>U</b>	<b>NA</b>	<b>U</b>
5. Include an evaluation of audit needs in every project paper and, if necessary, budget funds.	1988	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>	<b>U</b>
	1989	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>
6. Use competent accounting firms to perform audits, if required.	1988	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>NA</b>	<b>NA</b>	<b>S</b>	<b>U</b>
	1989	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>
7. Follow appropriate close out procedures.	1988	<b>U</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>S</b>	<b>S</b>	<b>S</b>	<b>U</b>
	1989	<b>S</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>U</b>	<b>S</b>	<b>U</b>

Legend

S - Satisfactory

U - Unsatisfactory

NA - Not applicable

Of the 47 instances where the missions rated their control techniques as "satisfactory" or "not applicable," we found that 21—or about 45 percent—of these cases should have been rated "unsatisfactory." Examples of areas where we disagreed with the mission's assessments are presented below.

- In 1988 and 1989, the AID missions in Bangladesh and Jordan rated host agency capability assessments (control technique 1 in table 1) as "satisfactory," despite the fact that neither mission could produce examples of assessments that were conducted.
- For both 1988 and 1989, the mission in Pakistan rated contract audit coverage for host country contracts (control technique 4 in table 1) as "not applicable" on the assumption that the Government of Pakistan audited all AID-financed host country contracts. The mission controller told us that the assessment was in error and that the mission did not rely on any Pakistani agency to provide required audits. In addition, due to the complete lack of documentation showing that host country contracts have been audited, this control technique should have been rated "unsatisfactory" in both years.

- In 1988, the Bangladesh mission rated contract close outs (control technique 7 in table 1) as "unsatisfactory" due to the lack of a written mission policy for either AID direct or host country contracts. In its 1989 assessment, the mission rated this control technique "satisfactory" because the mission had issued an order establishing AID direct contract close out procedures. However, at the time of our review the mission still did not have close out procedures for host country contracts, and we found no evidence that close out audits were being performed.

Although AID has reported the lack of capability assessments as a material weakness since 1983 and the lack of contract audits as a weakness since 1984, these and other internal control techniques relating to host country contracting were not correctly assessed at the missions we visited. Inaccurate reporting by these missions adversely affected AID/Washington's ability to monitor implementation of key oversight requirements for host country contracts and resulted in lost opportunities to correct mission-specific control weaknesses.

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## Recommendation

We recommend that the AID Administrator ensure that overseas missions provide complete and accurate reports on internal control weaknesses.

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## Scope and Methodology

We interviewed AID officials in Washington, D.C., and reviewed AID's policies and procedures for conducting internal controls assessments. We also interviewed AID officials located at missions in Bangladesh, Egypt, Jordan, and Pakistan. In each mission, we examined supporting documentation for internal control assessments of selected control techniques conducted in 1988 and 1989.

We did not obtain formal agency comments on this report, since we discussed the contents of the report with members of your staff, who agreed with the information presented. Our review was conducted between October 1989 and December 1990 in accordance with generally accepted government auditing standards.

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The head of a federal agency is required by 31 U.S.C. 720 to submit a written statement on actions taken on this recommendation to the Senate Committee on Governmental Affairs and the House Committee on Government Operations not later than 60 days after the date of the report and to the House and Senate Committees on Appropriations with

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the agency's first request for appropriations made more than 60 days after the date of the report.

We are sending copies of this report to the Chairman, Subcommittee on Oversight of Government Management, Senate Committee on Governmental Affairs; other appropriate congressional committees; and the Director, Office of Management and Budget. Copies will also be made available to others on request.

Major contributors to this report were Albert H. Huntington, III, Assistant Director; Michael ten Kate, Evaluator-in-Charge; and Evaluators John Nelson and Michael Rohrback. If you or your staff have any questions regarding this report, please call me on (202) 275-5790.

Sincerely yours,

A handwritten signature in black ink, appearing to read "Harold J. Johnson". The signature is fluid and cursive, with a large, stylized initial "H" and a long, sweeping underline.

Harold J. Johnson  
Director, Foreign Economic  
Assistance Issues